In the
Supreme Court of the United States

OCTOBER TERM A. D. 1940.

NO. 539 - 543

STATE OF MINNESOTA, Petitioner,

vs.

DULUTH, MISSABE AND NORTHERN RAILWAY COMPANY, and Duluth, Missabe and Iron Range Railway Company, Respondents.

NO._____

STATE OF MINNESOTA, Petitioner,

vs.

THE DULUTH AND IRON RANGE RAIL ROAD COMPANY and Duluth, Missabe and Iron Range Railway Company, Respondents.

NO._____

STATE OF MINNESOTA, Petitioner,

vs.

SPIRIT LAKE TRANSFER RAILWAY COMPANY and Duluth, Missabe and Iron Range Railway Company, Respondents.

NO._____

STATE OF MINNESOTA, Petitioner,

vs.

OLIVER IRON MINING COMPANY, Respondent.

NO._____

STATE OF MINNESOTA, Petitioner,

vs.

PROCTOR WATER & LIGHT COMPANY, Respondent.

PETITION OF WRITS OF CERTIORARI TO THE SUPREME COURT OF MINNESOTA AND BRIEF IN SUPPORT THEREOF

J. A. A. BURNQUIST,
Attorney General of the State of Minnesota,
102 State Capitol, St. Paul, Minnesota,
Counsel for Petitioner.

JOHN A. PEARSON,
Special Attorney for the State of Minnesota,
E-901 First Natl. Bank Building,
St. Paul, Minnesota,
IRVING M. FRISCH,
Special Attorney for the State of Minnesota,
416 Hodgson Building,
Minneapolis, Minnesota,
Of Counsel for Petitioner.

Court Printing Company, 322 So. 4th St., Minneapolis

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PETITION FOR WRITS OF CERTIORARI TO THE SUPREME COURT OF MINNESOTA.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States.

Your petitioner, the State of Minnesota, by its counsel, respectfully shows:

SUMMARY STATEMENT OF THE MATTER INVOLVED.

The legislature of Minnesota enacted Laws of 1933, Chapter 405[1] imposing on individuals and corporations "income taxes and franchise or privilege taxes measured by income."

The act has been sustained by the Minnesota Supreme Court against certain claims that it violated the equal protection and due process clauses of the Fourteenth Amendment to the United States Constitution and the uniformity clause of the Minnesota Constitution.[2]

The State of Minnesota brought five separate suits against the corporations above named for taxes under this act for the year 1933. The five actions were consolidated for trial in the state district court.

In the cases of the railroad company defendants it was asserted by defendants in their pleadings and in the state district and supreme courts that the imposition of the tax "would deprive this defendant, and said other railroad corporations, of their property without due process of law and deny to them the equal protection of the laws contrary to the provisions of the Fourteenth Amendment to the Constitution of the United States" and contrary to provisions of the Minnesota Constitution. These several contentions were denied by plaintiff.

The Minnesota Tax Commission assessed a tax against

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[1]This act in its original and amended forms is found in Volume 3, Cumulative Supplements to Mason's Minnesota Statutes, 1927, sections numbered 2394-1 et seq.

[2]Reed v. Bjornson, 191 Minnesota Reports 254, 253 Northwestern Reports 102; Thompson-Parker Holding Company v. Bjornson, 191 Minnesota 271, 253 Northwestern 110.

each corporation separately. The defendants in each case asserted in their pleadings and in the district and state supreme courts that they were entitled to have their taxes calculated on a consolidated basis including in such consolidation the net incomes or net deficits of 75 other subsidiaries of the United States Steel Corporation. Section 32 (c) of the Act[3] provided that under certain circumstances of corporate affiliation and control "the (Tax) Commission may impose a tax as though the combined entire taxable net income was that of one corporation". (Emphasis supplied.) Defendants asserted the claim that this provision was mandatory and that the failure of the Tax Commission to impose a tax on a consolidated basis was "an attempted exercise of a legislative function which has not been and cannot be delegated to said Commission." The statutory provision in its permissive form was asserted by defendants, in the district court and in the Minnesota Supreme Court, to "deny to this defendant and its said affiliated corporations the equal protection of the laws and would deprive them of their property without due process of law contrary to the provisions of the Fourteenth Amendment to the Constitution of the United States." The statutory provision was alleged by defendants to violate the uniformity clause of the Minnesota Constitution, Art. 9, Sec. 1, as well as Art. 3, prohibiting delegation of legislative powers to the Tax Commission. These contentions were denied by plaintiff.

The trial court upheld the claim of defendants that the railroad corporations were not taxable upon any part of their income whether "railroad income" or "non-railroad income." It held with the state that defendants were not entitled to be taxed on a consolidated

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[3]Vol. 3, Cumulative Supplements to Mason's Minnesota Statutes, 1927 Section 2394-32 (c).

basis and that the non-railroad defendants were subject to the tax.

The state appealed to the Minnesota Supreme Court in the railroad cases and the non-railroad defendants appealed in the other two cases. The three railroad cases were argued together December 7, 1939, and the other two cases were argued together the following day, December 8, 1939. Two opinions in the five cases were filed by the Minnesota Supreme Court December 29, 1939. Upon petitions for reargument one further opinion was filed in all five cases April 26, 1940.

These opinions are reported as **State v. Duluth, Missabe and Northern Railway Company,** 207 Minn. 618, 292 N. W. 401, **State v. Oliver Iron Mining Company,** 207 Minn. 630, 292 N. W. 407, and **State v. Duluth, Missabe and Northern Railway Company,** 207 Minn. 637, 292 N. W. 411.

The state supreme court held that "railroad income" was not taxable but that "non-railroad income" was taxable.

The state supreme court held that defendants were entitled to a consolidated basis of taxation; that to construe Section 32 (c) as permissive would be violative of the Fourteenth Amendment; and that failure to construe it as mandatory would be violative of the Fourteenth Amendment. We expect to show that the non-federal grounds given for the construction were not independent nor adequate to sustain the judgments on this point.

The statutory measure of the Minnesota Income and Franchise Tax Act of 1933 is net income. Net income consists of gross income less certain deductions.

In computing net income the Minnesota Tax Commission included in gross income of defendant Duluth Missabe and Northern Railway Company an amount of

$7,774,804.19 received by it from the United States in 1933. Defendants asserted in their pleadings and in the district and supreme courts of the state that this amount of $7,774,804.19 was not properly includable for computation in the tax and that said moneys received from the United States did not constitute income of this defendant taxable under the Minnesota Income and Franchise Tax Act.

Pursuant to the Transportation Act, Act of Congress of February 28, 1920, 41 Stat. 488, the defendant Duluth, Missabe and Northern Railway Company had transferred and paid to the United States for the years 1920, 1922, 1923, 1925, 1926, 1928 and 1929, the aggregate sum of $5,808,256.61. At the times of transfer and payment to the United States and thereafter defendant had no title legal or equitable, to these amounts. These amounts belonged to the United States.[4]

The defendant Duluth, Missabe and Northern Railway Company received said amount of $7,774,804.19 from the United States pursuant to Act of Congress of June 16, 1933, 48 Stat. 220. This act liquidated and distributed the moneys belonging to the United States held in the general railroad contingent fund accumulated pursuant to the said Transportation Act of 1920. Under the provisions of this Act the entire amount of $7,774,804.19 received by the defendant from the United States was expressly made subject to the payment of federal income taxes for the year 1933.

The Act of Congress of 1933 created this income as income in the hands of defendant Duluth, Missabe and Northern Railway Company. Prior thereto it was property of the United States. Without the Act of Congress there would have been no such income of defendant.

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[4]Dayton-Goose Creek R. Co. v. U. S., 263 U. S. 456, 44 S. Ct. 169, 68 L. ed. 388.

This sum of $7,774,804.19 is "non-railroad income" under the differentiation of "railroad" and "non-railroad income" fixed and established by the state supreme court under the Minnesota Income and Franchise Tax Act. It is the contention of petitioner that the Minnesota Supreme Court erroneously construed the Acts of Congress of February 28, 1920 and June 16, 1933, and failed to give effect to the decision of this court in the case of **Dayton-Goose Creek R. Co. v. U. S. supra,** and as a result thereof placed said amount of $7,774,804.19 in the category of "railroad income" instead of in the category of "non-railroad income."

The inclusion or exclusion of this amount in the measure of the tax makes a total difference of $388,740.21. This item constituted a substantial part of plaintiff's cause of action against Duluth, Missabe and Northern Railway Company.

It is the contention of petitioner that it is entitled to a correct construction of said Acts of Congress and that it is entitled to have the decision of this court in the case of **Dayton-Goose Creek R. Co. v. U. S., supra,** applied to said Acts of Congress.

The misconstruction by the state supreme court of the said acts of Congress and the misapplication of the statutory definition as construed by the court, destroyed not only an essential element of plaintiff's cause of action against the Duluth, Missabe and Northern Railway Company, but also, as we shall hereinafter more particularly point out, materially and substantially affected plaintiff's causes of action against the defendants in the other cases. This error in its application is common to all defendants in all of the above cases.

The state supreme court having held that defendants and the 75 other subsidiaries of the United States Steel Corporation were entitled to a consolidated basis of taxation, the necessary effect of the removal of this item of $7,774,804.19 from the total of gross income was to reduce the total combined income to a point where, with other deductions made by the supreme court, the entire tax was wiped out against all the corporations.

The state also included in the measure of the franchise tax sought to be collected from the defendants interest from federal securities which in the case of the Duluth, Missabe and Northern Railway Company amounted to $150,044.12 and in the case of The Duluth and Iron Range Railroad Company $214,066.12. These defendants claim that this income could not be included in the measure of their tax because it was immune from taxation under the federal constitution, Acts of Congress, and the Minnesota statute. The state on the other hand contended that this income was properly included in the measure of defendants corporate franchise tax under the provisions of Section 12 of said Act which included in gross income income from all securities of every description whatsoever with the **sole exception** of securities of the State of Minnesota and its local governmental subdivisions.

The Minnesota Supreme Court decided in favor of defendants on this point. The reason given by the court for its decision was that the inclusion of income from federal securities in the measure of the Minnesota Corporate Franchise tax constituted an "unfriendly discrimination" against the United States in favor of local securities in "substantial competition" with federal securities and was therefore unconstitutional.

There was also a non-federal ground given by the court for its decision. However, as demonstrated in

the jurisdictional statement herein, page 36 infra, this was the result of the court having completely overlooked subdivision (*l*) of Section 12 of the Minnesota statute which expressly included interest from federal securities in the measure of the tax. The circumstances connected with the overlooking of this subdivision (*l*) by the court are fully set forth in the jurisdictional statement, Section C.

The date of the judgments sought to be reviewed in these cases is June 13, 1940. The mandates to the trial court have been stayed pending proposed review by this court.

The time for making application for a writ of certiorari in each of the above entitled cases was on September 9, 1940 extended for a period of thirty days from September 12, 1940, by order of Mr. Justice Black. On October 7, 1940, a further extension for a period of twenty days from October 12, 1940, was made by order of Mr. Justice Reed.

The statutory provisions believed to sustain the jurisdiction of the Supreme Court of the United States to review by writ of certiorari the judgments of the Supreme Court of Minnesota is Section 237 (b) of the Judicial Code, as amended, United States Code Annotated, Title 28, Section 344 (b), which provides:

> "It shall be competent for the Supreme Court, by certiorari, to require that there be certified to it for review and determination, with the same power and authority and with like effect as if brought up by writ of error, any cause wherein final judgment or decree has been rendered or passed by the highest court of a State in which a decision could be had * * * where is drawn in question the validity of a statute of any State on the ground of its being repugnant to the Constitution, * * * or laws of the United States, or where any title, right, privilege, or immunity is specially set up or claimed by either party under the Constitution, or any * * * statute of, * * * or authority exercised under the

United States; and the power to review under this paragraph may be exercised as well where the Federal claim is sustained as where it is denied. * * *"

It is the contention of petitioner that the above entitled actions, and each of them, involve, and there is drawn in question in the above entitled actions, and each of them, the rights specially set up and claimed by petitioner under the Constitution of the United States and amendments thereof, and under those certain statutes of the United States, and each of them, to-wit, Act of Congress of February 28, 1920, 41 Stat. 488, Chapter 91, and especially Section 422 thereof, Title 49, United States Code Annotated, Section 15 a, and Act of Congress of June 16, 1933, 48 Stat. 220, Chapter 91, and especially Title II, Section 206, thereof, Title 49, United States Code Annotated, Section 15 b, and under the authority exercised thereunder.

There is further drawn in question in the above entitled actions, and each of them, the validity of said statute of the State of Minnesota, namely, Chapter 405, Laws of Minnesota 1933, and especially Section 32 and subsection 32 (c) thereof in the form in which the legislature enacted said chapter and section on the ground of its being repugnant to the Constitution of the United States and the amendments thereof, especially the Fourteenth Amendment, Section 1, and the due process and equal protection clauses thereof.

There is also drawn in question in the above-entitled actions and each of them the validity of Section 12 of said statute, Chapter 405, on the ground of its being repugnant to the immunity of federal securities from taxation by the states under the Constitution of the United States.

Relevant excerpts from Chapter 405, Laws Minnesota 1933 are set forth in the Appendix hereto as Exhibit A.

The date upon which the application for writ of certiorari herein is presented is November 1, 1940.

STATEMENT PARTICULARLY DISCLOSING THE BASIS UPON WHICH IT IS CONTENDED THAT THIS COURT HAS JURISDICTION TO REVIEW THE JUDGMENTS IN QUESTION.

For the convenience of the court we have divided the jurisdictional statement into three parts: Section A, relating to payments to defendant Duluth, Missabe and Northern Railway Company by the United States under Act of Congress of June 16, 1933; Section B, relating to taxation of affiliated corporations on a combined basis; and Section C, relating to inclusion of interest from federal securities in the measure of the Minnesota Corporate Franchise Tax Act.

Section A. Payments to defendant Duluth, Missabe and Northern Railway Company by the United States under Act of Congress of June 16, 1933.

There is drawn in question in the above entitled actions, and each of them, the rights specially set up and claimed by petitioner under the Constitution of the United States and amendments thereof, and under certain acts of Congress, namely, Act of Congress of February 28, 1920, 41 Stat. 488, and Act of Congress of June 16, 1933, 48 Stat. 220, and authority exercised under the United States. Judicial Code, as amended, Section 237 (b), quoted above.

Relevant excerpts of these Acts of Congress are set forth in the Appendix as Exhibits B and C, respectively.

The plaintiff's cause of action against each defend-

ant is measured by the net income of defendant in each case. The net income is governed by the amount of gross income because net income is gross income less certain statutory deductions. Thus the amount of gross income has a determining effect upon the amount of the tax which is 5% of the net income less certain specific statutory deductions.

In the case against the defendant Duluth, Missabe and Northern Railway Company, the moneys received by it from the United States in 1933 amounting to $7,774,804.19 directly affect plaintiff's cause of action against that company and determine its cause of action to the extent of $388,740.21. The amount of gross income is an essential element of plaintiff's cause of action.

This portion of defendant's gross income and this element of plaintiff's cause of action was created by, and the nature of the element determined by, the Acts of Congress above referred to.

The other defendants except Duluth, Missabe and Iron Range Railway Company and Spirit Lake Transfer Railway Company are affected by the inclusion or exclusion of this amount in connection with defendants' claim of right to be taxed on a consolidated basis. This relationship will be developed in Section B hereof.

The defendant Duluth, Missabe and Iron Range Railway Company is affected as a successor in interest of the other three railroad corporations. The allocation of income on a combined basis is or may be affected by Spirit Lake Transfer Railway Company. All are Minnesota corporations.

Under the Minnesota Income and Franchise Tax Act, Chapter 405, Laws of Minnesota 1933, "non-railroad income", i. e., "income derived from the exercise of the corporate franchise without the scope of railroad owner-

ship or operation" is includable in the measure of the tax.

It was and is the contention of petitioner that the said $7,774,804.19 received by defendant Duluth, Missabe and Northern Railway Company from the United States was non-railroad income under the above definition of non-railroad income fixed and established by the Minnesota Income and Franchise Tax Act as construed by the state supreme court.

This contention of petitioner is discussed in the annexed Brief, pages 50 et seq., and for the sake of brevity our argument in that connection will not be repeated here.

At page 51, et seq., we discuss "differentiation of income under the Minnesota Income and Franchise Tax Act as construed by the state supreme court."

Under this differentiation income derived from the exercise of the corporate franchise **without** the scope of railroad ownership or operation is non-railroad income. See page 51, et seq., of the accompanying Brief.

The corporate franchise was not exercised for railroad purposes in the acquisition of the $7,774,804.19 from the United States. Page 53, et seq.

The state supreme court determined that all of the money received by the Duluth, Missabe and Northern Railway Company from the United States was railroad income.

The state contends that this was an erroneous construction and conclusion and involved an erroneous interpretation of the Acts of Congress of June 16, 1933, and of February 28, 1920, respectively, 48 Stat. 220 and 41 Stat. 488, and that such construction and conclusion involved a failure of the state supreme court to follow the decision of the United States Supreme Court construing said Act of Congress of 1920 in **Dayton-Goose Creek R. Co. v. U. S., supra.**

It is the contention of the petitioner that if the state supreme court construes an act of Congress expressly or by necessary intendment, then it must construe it properly and a failure to construe it properly raises a federal question. It is the contention of the state that the above-mentioned Acts of Congress are necessarily involved in defining and determining plaintiff's causes of action.

It is the further contention of petitioner that the state supreme court expressly or by necessary intendment passed upon petitioner's federal claims relating to the Acts of Congress above referred to. As we understand the rule of this court, if the state supreme court expressly passed upon petitioner's claims, it is immaterial how or when the federal claims were raised in the state supreme court.

However, defendants at all stages of the litigation, in the pleadings and at the trial and in the state supreme court, asserted the federal grounds alleged to be involved, namely, that taxation of the railroad corporations and their income, including the taxation of the $7,774,804.19 received by defendant Duluth, Missabe and Northern Railway Company from the United States in 1933 pursuant to the Acts of Congress of 1933 and 1920, violated their rights under the Constitution of the United States and under said Acts of Congress.

At page 293 Record, Case No. 32125 in paragraph 10 of Answer (Substituted) of the Duluth, Missabe and Northern Railway Company defendant alleged that the said $7,774,804.19 (amount itemized: $5,808.256.61; $1,817,163.52; $149,384.06) "* * * represent moneys received by the taxpayer from the United States Government under the provisions of the Acts of Congress of June 16, 1933, being chapter 91, Title II, section 206, 48 Stat. 220, that such moneys do not constitute income

of this defendant taxable under the Minnesota State Income Tax Act among other reasons because they constitute a gift from the United States Government, an instrumentality of the United States Government and/or income earned by the taxpayer in previous years."

In paragraph 12 of said Answer (Substituted) page 293 Record, Case No. 32125 defendant alleged "* * * that prior to the year 1933 it paid to the Interstate Commerce Commission, under the provisions of the so-called Recapture Clause of the Transportation Act of 1920, 41 Stat. 489, the aggregate sum of $5,808,256.81 * * *". This amount is the same sum referred to in paragraph 10 as part of the $7,774,804.19 received by defendant from the United States in 1933.

Defendants' assertion of federal rights were contentions on their part with respect to the essential elements of plaintiff's causes of action.[5] Plaintiff's causes of action did not change. The federal elements existed from the beginning.

Plaintiff in Exhibit 2 attached to its Statement (Complaint) Record page 35, Case No. 32125, specified the $5,808,256.61 principal of the recapture fund above referred to and the $1,817,163.52 of the accretions referred to, the remainder of the accretions amounting to $149,384.06 having been included in defendant's tax return. See Record page 293, paragraph 10 supra where defendant refers to this amount as having been erroneously reported as taxable income. And see Exhibit S-1 (b) Record page 87 where this amount is referred to as "accretions to recapture fund included as income in return and now claimed to be non-taxable by tax payer $149,384.06."

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[5]Cf. Jones National Bank v. Yates, 240 U. S. 541, 36 S. Ct. 429, at pages 432, 433, 60 L. ed. 788.

Although it is petitioner's contention as asserted above that the state supreme court expressly passed upon its federal claims relating to the Acts of Congress of 1933 and 1920 and the authority exercised under the United States by virtue of said Acts, the federal questions relating to the moneys paid by the United States and the construction and application of the Acts of Congress were duly raised and specially set up in plaintiff's petitions for rehearing and reargument in these cases in the state supreme court prior to the decision of April 26, 1940, 207 Minn. 637, 292 N. W. 411, and long prior to the judgments herein. In its Reply and Supplement to State's Petitions for Rehearing and Reargument duly filed in a section entitled, "This Court by Its Decisions Relating to the Principal Amount of Recapture Fund has Misconstrued and Misinterpreted the Acts of Congress of 1920 and 1933, 41 Stat. 488 and 48 Stat. 220, and the Construction of the 1920 Act by the United States Supreme Court and Thereby Denied to Plaintiff Rights under the Constitution of the United States and under said Acts of Congress" and elsewhere in that document filed March 16, 1940, pursuant to permission of the court these federal questions were discussed and specially set up both as to the so-called principal of the recapture fund amounting to $5,808,256.61 and as to the so-called accretions to the fund amounting to $1,966,547.58.

This, as above stated, was all prior to any judgments in the state supreme court. Plaintiff's supplement to its rehearing petitions served on defendants March 15, 1940, filed March 16, 1940, was answered by defendants March 21, 1940, in an Answer in which defendants did not controvert plaintiff's arguments on the federal questions but said at page 9 thereof: "Other points made by the state are simply restatements of argu-

ments already made and have been answered by our earlier briefs."

It was following plaintiff's petitions for rehearing and reargument and the said supplement thereto that the state supreme court's decision of April 26, 1940, was rendered, 207 Minn. 637 and 292 N. W. 411. The judgments in the state supreme court were not rendered until June 13, 1940.

The court in its decision on the Petitions for Rehearing and Reargument, April 26, 1940, reiterated its position on the recapture funds, principal as well as accretions, and at 207 Minn., pages 639, 640, 292 N. W., at pages 412, 413, paid special attention to the accretions amounting to $1,966,547.58.

In this decision of April 26, 1940, the court further, 207 Minn., at page 639, 292 N. W., at page 412, construed and defined the Minnesota Income and Franchise Tax Act of 1933 making it clear that the distinction between railroad and non-railroad income under that Act lay "between income derived from the exercise of the franchise within the scope of railroad ownership or operation and that from its exercise without such scope." This definition, as we point out in more detail later in our Brief, placed the $7,774,804.19 payment from the United States in the category of non-railroad income.

Petitioner contends not only that its federal claims relating to the Acts of Congress of 1920 and 1933 were expressly passed upon in the court's decisions of December 29, 1939, but also that these claims were expressly passed upon by the court in its decision of April 26, 1940, following the Petitions for Rehearing and Supplement thereto.

The state supreme court in its decision of December 29, 1939, as we more fully point out under Points I and II of our Brief failed to give due effect to the Act of Con-

gress of 1933, failed to properly construe said Act, failed to give due effect to the Act of Congress of 1920, failed to properly construe said Act, and failed to give due effect to the decision of the United States Supreme Court in the case of **Dayton-Goose Creek R. Co. v. United States, supra.** The result of this misconstruction was that the payment of $7,774,804.19 made by the United States to defendant pursuant to the Act of 1933 out of moneys belonging to the United States accumulated in connection with the Act of 1920 were treated as if they were railroad earnings received by the Duluth, Missabe and Northern Railway Company in the ordinary course of its transportation business. We especially call attention to that part of the decision of December 29, 1939, 207 Minn. 618, at pages 624, 625, 292 N. W. 401, at page 405, quoted at pages 51, 52 of Brief, infra.

The rights of petitioner specially set up passed on by the state supreme court and denied to petitioner by the state supreme court include the following:

Plaintiff was entitled to have all non-railroad income included as part of its cause of action against the Duluth, Missabe and Northern Railway Company, against its successor and against the other defendants in the other four cases.

A correct interpretation or application of the Acts of Congress would result in placing the payments made by the United States in the non-railroad category. **Plaintiff was entitled to a correct construction and application of the Acts of Congress. A correct construction and application of the Acts of Congress would have avoided the denial of plaintiff's rights in these respects.** A correct construction and application of the Acts of Congress would have resulted in recognition of the complete cut-off and severance of the title and interest of the Duluth Missabe and Northern Railway

Company in and to the funds in the general railroad contingent fund, and would have resulted in the recognition of the $7,774,804.19 as non-railroad income. It will be observed that the money was treated as income but it was treated as the wrong kind of income and the applicable definitions and principles governing the differentiation of the income were ignored.

Plaintiff was entitled under the Act of Congress of 1920 to have the state supreme court take account of that act and of the decision of this court construing it in the Dayton-Goose Creek case, and plaintiff was entitled to have the state court recognize the complete cut-off and severance of the payments made by defendant, Duluth, Missabe and Northern, to the United States in the years 1922 to 1929 amounting to $5,808,256.61. Had the court done so it would have found it impossible to say, as above quoted, 207 Minn. at page 625, 292 N. W. at page 405, that "the repayment amounts to nothing more than the return to defendants of their own railroad earnings. The restoration reinstated the earnings in their original status."[6] It was obviously impossible to thus unscramble the transactions from 1920 to 1929. Or if it had said so, it could have made this statement only in a figurative sense and without attaching thereto any meaning which would have a bearing on the proper description of the funds with reference to the proper income category as laid down in its established definition and principle of differentiation. The state supreme court's fixed and established definition and principle of differentiation was definitively stated by the state supreme court in 207 Minnesota, at page 639, 292 Northwestern, at page 412, supra, as "the distinction (between railroad and non-railroad income) should lie

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[6]207 Minn. 618, 625, 292 N. W. 401, 405.

between **Income derived from the exercise of the (corporate) franchise within the scope of railroad ownership or operation and that from its exercise without such scope.**" (Emphasis and parentheses supplied.)

Plaintiff was entitled under the Act of Congress of 1933 to have the state supreme court hold and recognize that the receipt by defendant of $7,774,804.19 from the United States in 1933 was solely as a result of the Act of Congress and that defendant owed the receipt of the money solely and entirely to the distribution made by Congress and not at all to any exercise of the corporate franchise by defendant for railroad purposes.

Plaintiff was further entitled to have the supreme court hold that the Act of 1933 was confirmatory of the complete cut-off and severance of defendant's title and interest, legal and equitable, in the sum of $5,808,256.61. Plaintiff was further entitled to have the state supreme court hold that the accretions amounting to $1,966,-547.58, had not even passed through the hands of defendant until the distribution by Congress in 1933.

Recognition of these considerations would have prevented the conclusion above quoted that "the restoration reinstated the earnings in their original status."

In the case of **Jones National Bank v. Yates, supra,** 240 U. S. 541, 36 S. Ct. 429, at page 433, 60 L. ed. 788, this court said with respect to defining the liability of national bank directors that if the plaintiffs' cause of action required the application of the federal statute in defining the liability with respect to the acts alleged and proved, the plaintiffs were entitled to the correct application of the federal statute.

Likewise in the instant cases, if the state's cause of action against Duluth, Missabe and Northern Railway Company required the application of the Acts of Con-

gress in defining the liability of defendant, the state was entitled to their correct application.

The correct construction and application of the Acts of Congress vitally affected each of plaintiff's causes of action.

Denial of such construction and application deprived plaintiff of valuable rights under the United States Constitution, under said Acts of Congress and under the authority of the United States.

We call attention to the fact that we do not have here a case where the state legislature undertook to characterize as "railroad income" certain income which was not such in fact.[7]

The **definition** of non-railroad income when applied to the **fact** of income leaves no room for doubt of the result, namely, that the $7,774,804.19 received by defendant, Duluth, Missabe and Northern is non-railroad income under the Minnesota statute.

The **definition** cannot be misconstrued or misapplied without violating plaintiff's rights under the Acts of Congress. Plaintiff is entitled to have the definition applied like any other litigant.

The **facts** cannot be ignored or misconstrued without violating plaintiff's rights under the Acts of Congress. If the method of treatment employed by the state supreme court be held to result in an adequate non-federal ground, then the construction and application of federal statutes may be entirely circumvented.

There is a good deal in the state supreme court's opinions, both in the first opinion in the railroad cases and in the last opinion of April 26, 1940, which furnishes grounds for the view that that court ignored the facts of the income. The court said: "The restoration rein-

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[7]Cf. Tyler v. United States, 281 U. S. 497, 50 S. Ct. 356, 74 L. ed. 991, 69 A. L. R. 758.

stated the earnings in their original status." Such unscrambling could, of course, not take place and at most the expression might serve a rhetorical purpose. This treatment simply ignored the facts and applied the definition of non-railroad income as if the income had been ordinary railroad income. If the facts were ignored a federal question is involved, because the facts of the income were dependent upon the Acts of Congress. Their very nature were created by Congress.

If, however, the state court recognized that the money was income received from the United States but treated it as not different, for example, from money received from the United States for transportation of the mails, then the facts remained distorted because this payment was different from payment for transportation of the mails and a federal question was involved. To treat it as the same would ignore the Acts of Congress of 1920 and 1933, as well as the decision of this court interpreting the former act.

Conceivably the state court might have recognized and considered the true nature of the facts of the income and might have taken cognizance of the Acts of Congress but misconstrued the Acts of Congress or misapplied them. In any event a federal question remained.

The United States Supreme Court is not concluded by the findings of fact or by a mixed finding of law and fact made by the state court. **Great Northern Ry. Co. v. Washington,** 57 S. Ct. 397, 300 U. S. 154, 81 L. Ed. 573. This court, at 57 Supreme Court, page 403, 300 U. S. page 166, quoting from the case of **Norris v. Alabama,** 55 S. Ct. 579, 294 U. S. 587, 79 L. ed. 1074, which involved a question of fact, said:

> "That the question is one of fact does not relieve us of the duty to determine whether in truth a federal right has been denied. When a federal right has been specially set up and claimed in a state

court, it is our province to inquire not merely whether it was denied in express terms but also whether it was denied in substance and effect. If this requires an examination of evidence, that examination must be made. Otherwise, review by this Court would fail of its purpose in safeguarding constitutional rights. Thus, whenever a conclusion of law of a state court as to a federal right and findings of fact are so intermingled that the latter control the former, it is incumbent upon us to analyze the facts in order that the appropriate enforcement of the federal right may be assured."

The following additional fact cases were cited in the case of **Great Northern Railway Company v. Washington, supra:**

Beidler v. South Carolina Tax Commission, 51 S. Ct. 54, 282 U. S. 1, 75 L. ed. 131;

Johnson Oil Company v. Oklahoma, 54 S. Ct. 152, 290 U. S. 158, 78 L. ed. 238.

This court further said, 57 S. Ct. at page 404, 300 U. S. at page 167:

"Citation of authority for the same principle might be multiplied indefinitely."

If the view be taken that the state supreme court merely declined to pass on the facts to which the statutory principle was to be applied, or declined to pass on the Acts of Congress involved, the federal question would not thus be avoided.

"* * * But the Constitution, which guarantees rights and immunities to the citizen, likewise insures to him the privilege of having those rights and immunities judicially declared and protected when such judicial action is properly invoked. Even though the claimed constitutional protection be denied on nonfederal grounds, it is the province of this Court to inquire whether the decision of the state court rests upon a fair or substantial basis. If un-

substantial, constitutional obligations may not be thus avoided."

Lawrence v. State Tax Commission of Mississippi, 52 S. Ct. 556, 558, 286 U. S. 276, 282, 76 L. ed. 1102, 87 A. L. R. 374.

"Where a federal right is concerned we are not bound by the characterization given to a state tax by state courts or Legislatures, or relieved by it from the duty of considering the real nature of the tax and its effect upon the federal right asserted."

Carpenter v. Shaw, 50 S. Ct. 121, 123 280 U. S. 363, 7, 8, 74 L. ed. 478.

In the case of **Ancient Egyptian Arabic Order of Nobles of Mystic Shrine v. Michaux**, 49 S. Ct. 485, 279 U. S. 737, 73 L. ed. 931, a Texas court held that facts showed no laches as pleaded by defendant and in this court such ruling was held not to avoid the federal question. This court reviewed the evidence and held that laches occurred and reversed the state court.

A similar case was **Creswill v. Grand Lodge Knights of Pythias of Georgia**, 32 S. Ct. 822, 225 U. S. 246, 56 L. ed. 1074. In that case a jury had a Georgia court held that no acquiescence or laches existed in fact. This court reviewed the evidence and came to a conclusion on the facts contrary to that of the Georgia court and reversed the judgment.

We believe there can be no question of the nature of the facts to which the definition of the Minnesota statute is to be applied. However, if any such question be deemed to exist, then there are ample precedents of this court for inquiring into the facts to determine if a federal question is involved and to determine if an adequate non-federal ground exists.

The principal, if not the only, supposed non-federal ground given by the state court in support of its deci-

sion in this connection is that "the restoration reinstated the earnings in their original status." 207 Minn. at page 625, 292 N. W. at page 405, supra. As stated in the record page 74, they were earnings as follows:

"Date of Payment	For the Year	Amount of Payment
	1920	$620,000.00
	1922	89,000.00
	1923	2,142,000.00
May 5, 1924		$2,851,000.00
April 27, 1926	1925	545,892.85
April 25, 1927	1926	366,777.60
April 26, 1929	1928	364,780.35
April 29, 1930	1929	1,679,805.81
Total		$5,808,256.61"

We repeat that this is not a case where the state legislature undertook to characterize as "railroad income" certain income which was not such in fact. In the absence of any such characterization petitioner is entitled to have the statutory definition of non-railroad income applied to the facts as they exist.

We submit that this supposed non-federal ground is as wholly inadequate as was the state court's holding of voluntary payment as a non-federal ground in **Ward v. County Comrs of Love County,** 40 S. Ct. 419, 253 U. S. 17, 66 L. ed. 751, or the state court's holding of no laches in the Creswill case, supra.

In the Ward case just cited the state supreme court misconstrued petitioner's right under a real property exemption provided under Indian treaty stipulations. This court said at 40 S. Ct., page 421, 253 U. S., at page 22,

> "The right to the exemption was a federal right, and was specially set up and claimed as such in the petition. Whether the right was denied, or not given due recognition, by the Supreme Court is a question

> as to which the claimants were entitled to invoke our judgment, and this they have done in the appropriate way. It therefore is within our province to inquire not only whether the right was denied in express terms, but also whether it was denied in substance and effect, as by putting forward nonfederal grounds of decision that were without any fair or substantial support." (cases cited) "Of course, if nonfederal grounds, plainly untenable, may be thus put forward successfully, our power to review easily may be avoided". (Case cited)

In **Davis v. Wechsler,** 44 S. Ct. 13, 263 U. S. 22, 68 L. ed. 143 the federal right involved was the right of petitioner to venue as determined by a regulation of the director general of railroads under an act of Congress. The state court treated the regulation as having been waived by appearance. But this court said that the effect of the act of Congress and of the general order of the director general could not thus be avoided. This court said, 44 S. Ct. 14, 263 U. S. 24:

> "If the constitution and laws of the United States are to be enforced this court cannot accept as final the decision of the state tribunal as to what are the facts alleged to give rise to the right or to bar the assertion of it even upon local grounds."

In the interest of brevity, we refer to our Summary at the beginning of Points I and II of Brief, page 48.

Section B. Taxation of affiliated corporations on a combined basis.

There is drawn in question in the above-entitled actions, and each of them, the validity of a statute of the State of Minnesota, namely, Chapter 405, Laws of Minnesota 1933, and especially Section 32 and sub-section (c) thereof in the form in which the legislature enacted said chapter and said section, on the ground of its being repugnant to the Constitution of the United States and amendments thereof, especially the Four-

teenth Amendment, Section 1, and the equal protection clause thereof.

In the Appendix, Exhibit A, we have set forth relevant excerpts from Chapter 405, Laws Minnesota 1933.

The disputed sentence of Section 32 (c) is for convenience repeated here:

> "If 90% of all the voting stock of two or more corporations is owned by or under the legally enforceable control of the same interests the Commission **may** impose the tax as though the combined entire taxable net income was that of one corporation except that the credit provided by Section 27 (e) shall be allowed for each corporation; but intercompany dividends shall in that event be excluded in computing taxable net income." (Emphasis supplied.)

The state supreme court treated this statutory provision as a penalty and not as an aid in arriving at true taxable income. The court said in the Oliver case, 207 Minn. 630, at page 636, 292 N. W. 407, at pages 410, 411:

> "Without defining the conditions which the commission must find before it could impose a penalty, the legislature could not, as the state claims, leave the imposition of the penalty to the discretion of the commission. There would be an unconstitutional delegation of legislative powers. A. L. A. Schechter Poultry Corp. v. United States, 295 U. S. 495, 55 S. Ct. 837, 79 L. ed. 1570, 97 A. L. R. 947. There would also be a lack of uniformity which would violate our constitutional requirements (Minn. Const. art. 9, sec. 1, as well as U. S. Const. Amend. XIV) if discrimination resulted. We therefore give the statute an interpretation in harmony with the constitution."

The syllabus prepared by the court, No. 3, at page 630 is as follows:

> "It would be an unconstitutional delegation of legislative power to authorize the tax commission in its discretion to impose a penalty without a legislative definition of the conditions which it must find to exist before such penalty could be assessed. And

> if the imposition of the penalty be left to the uncontrolled discretion of the commission and resulted in discrimination, it would be a violation of our constitutional uniformity clause and of the XIVth amendment."

An analysis of the court's decision as we demonstrate in our Brief shows that the court was of the opinion that the purported penalty was left to the uncontrolled discretion of the commission because no conditions were defined in the statute "which the commission must find before it could impose" the penalty. Likewise since it was a "discretionary penalty" discrimination would inevitably result whenever the discretion to impose the penalty was exercised by the commission. This made it necessary in the eyes of the court to give the statute an interpretation in harmony with the Fourteenth Amendment. This the court proceeded to do by giving an **unnatural** meaning instead of a **natural** meaning to the permissive word "may" in Section 32 (c).

Section 32 (c) has been treated in the instant cases as if it were similar to the ordinance held violative of the equal protection clause of the Fourteenth Amendment in the case of **Yick Wo v. Hopkins**, 6 S. Ct. 1064, 118 U. S. 356, 30 L. ed. 220. In that case an ordinance of the City of San Francisco gave the Board of Supervisors authority at their discretion to refuse permission to carry on laundries except where located in buildings of brick or stone. This court said, 6 S. Ct. at page 1070, 118 U. S. at page 366, 30 L. ed. at pages 225-226:

> "* * *. It does not prescribe a rule and conditions, for the regulation of the use of property for laundry purposes, to which all similarly situated may conform. It allows, without restriction, the use for such purposes of buildings of brick or stone; but, as to wooden buildings, constituting nearly all those in previous use, it divides the owners or occupiers into two classes, not having respect to their personal character and qualifications for the business,

> nor the situation and nature and adaptation of the buildings themselves, but merely by an **arbitrary** line, on one side of which are those who are permitted to pursue their industry by the **mere will and consent** of the supervisors, and on the other those from whom that consent is withheld, at their **mere will and pleasure.** And both classes are alike only in this: that they are tenants at will, under the supervisors, of their means of living." (Emphasis supplied.)

In the interest of brevity and to avoid repetition we here summarize facts and arguments from Point III of our Brief, infra.

The state supreme court held that Chapter 405, Section 32 in the form in which it was enacted by the legislature is violative of the Fourteenth Amendment, Section 1, the equal protection clause being referred to by necessary intendment.

The Tax Commission in these cases levied the tax separately. The trial court sustained this holding.

The state supreme court erroneously ruled that Section 32 (c) was a penalty instead of a tax provision.

Statutory provisions similar to Section 32 (c) are common in state and federal tax laws. The cases from state courts and from lower federal courts cited in our Brief show that discretionary provisions for consolidated returns in the case of affiliated corporations are looked upon with favor by the courts. Such provisions are modern devices for coping with intricate corporate organizations.

Nowhere have we found any decision of the Supreme Court of the United States holding that such tax provisions are repugnant to Section 1 of the Fourteenth Amendment of the Constitution of the United States.

The state supreme court advanced several non-federal grounds for its decision on the points here involved.

None of these grounds are adequate to support the court's decision. Page 76, et seq., Brief.

The following two grounds are based on the State Constitution.

The Minnesota constitutional provision against delegation of legislative powers (Const. Art. 3) is neither an adequate nor an independent ground for invalidating Section 32 (c) in the form in which the legislature enacted it. Page 76, et seq., Brief.

The state uniformity clause, Art. 9, Sec. 1, is neither an adequate nor an independent ground for invalidating Section 32 (c) in the form in which the legislature enacted it.

The state uniformity clause is identical with the equal protection clause of Section 1 of the Fourteenth Amendment.

According to the Minnesota court, the natural permissive interpretation of the word "may" is violative of the Fourteenth Amendment because in its permissive form it provides for the imposition of a penalty without defining the conditions which the commission must find before it could impose a penalty. Therefore, says the court, it is a violation of the "uniformity clause" of the state constitution. Therefore, says the court, it is also an unconstitutional delegation of legislative power.

However, if the natural permissive interpretation of the word "may" does not amount to a grant of power to impose a discretionary penalty, this provision is not violative of the Fourteenth Amendment. Therefore, it is not violative of the "uniformity clause" of the state constitution. Therefore also, it is not an unconstitutional delegation of legislative power.

Thus the rationale for all the constitutional objections, state as well as federal, breaks down when once it is de-

termined that the natural permissive interpretation of the word "may" is not a grant of discretionary power to impose a penalty.

The two non-constitutional grounds given by the court were intended as a necessary alternative to what it believed would be an interpretation of this provision rendering it unconstitutional. Only under the compulsion of such necessity was the court driven to giving the word "may" a mandatory instead of its natural permissive meaning. Because of such compulsion and because of such assumed necessity, the non-constitutional grounds cannot be treated as independent. This is more fully set forth in our Brief, infra.

The statutory construction of Section 32 (c) based on Wisconsin legislative history is neither an adequate nor an independent ground for invalidating Section 32 (c) in the form in which the legislature of Minnesota enacted it. The court said, 207 Minnesota at page 634, 292 Northwestern at page 410:

> "It seems obvious that with that litigation in mind the Minnesota legislature attached the last sentence of subd. (c) for the purpose of making the powers and duties of the Minnesota tax commission clear; that it sought to give the Minnesota commission the power the Wisconsin commission claimed."

We agree with the Minnesota Supreme Court that the Minnesota legislature sought to give the Minnesota Tax Commission the powers that "the Wisconsin Commission claimed". However, it is clear that the Wisconsin Tax Commission never contended for a restriction of its powers. On the contrary it contended for expansion of its powers. What the Wisconsin Commission claimed was discretionary power to tax affiliated corporations upon a consolidated basis in cases where the facts were similar to those in the Curtis case. Curtis Company v. Wisconsin Tax Commission, 214 Wis. 85, 251 N. W. 497,

92 A. L. R. 1065. A careful study of the Wisconsin cases cited by the Minnesota court in its decision makes this very clear.

The statutory construction of Section 32 (c) based on the intention of the Minnesota Legislature to confer a power to be exercised for the benefit of the state or of a private party is neither an adequate nor an independent ground for invalidating Section 32 (c) in the form in which the legislature enacted it.

Nowhere does the court state or point out that the alleged benefit is for a private party.

The fact that the state does not derive any benefit from the mandatory taxation of affiliated corporations on a combined basis is fully demonstrated in our Brief, page 82, et seq.

The State questions in these cases are so interwoven with the Federal question as not to be independent matters.

Not only were none of the non-federal grounds suggested by the state court adequate to support the charge of unconstitutionality of Section 32 (c) but the questions, state and federal, were so interwoven as not to furnish an independent basis of decision on the points here involved.

We submit that there is more uncertainty in regard to the basis of the present decisions on the points here involved than was the case in **Minnesota v. National Tea Company**, 60 S. Ct. 678, 309 U. S. 551. In that case this court said, 60 S. Ct. at page 679, quoting from **State Tax Commission v. Van Cott**, 59 S. Ct. 605, 606, 306 U. S. 511, 514, 83 L. ed. 950:

> "* * * if the State court did in fact intend alternatively to base its decision upon the State statute and upon an immunity it thought granted by the Constitution as interpreted by this Court, these two

> grounds are so interwoven that we are unable to conclude that the judgment rests upon an independent interpretation of the State law."

As this court said in the next paragraph of the National Tea Company case (60 S. Ct. 679):

> "The procedure in those (sic) case was to vacate the judgment and to remand the cause for further proceedings, so that the federal question might be dissected out or the state and federal questions clearly separated."

In **Minnesota v. National Tea Company**, 60 S. Ct. 676, supra, this court vacated the judgment in order that the federal questions might be dissected out or the state and federal questions clearly separated and remanded the case for further proceedings.[8]

Section C. Inclusion of interest from federal securities in the measure of the Minnesota Corporate Franchise Tax.

There is drawn in question in the above-entitled actions of the State of Minnesota against Duluth, Missabe and Northern Railway Company et al. and The Duluth and Iron Range Railroad Company et al., the validity of a statute of the State of Minnesota, namely, Chapter 405, Laws of 1933, Section 12, which provides for the inclusion of income from federal securities, together with income from all other securities, with the sole exception of income from Minnesota state and local securities, in the measure of the Minnesota Corporate Franchise Tax, on the ground that it is repugnant to the federal constitutional immunity of federal securities from taxation by the states.

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[8]Following the remanding of the case by this court the Minnesota Supreme Court September 27, 1940, filed a per curiam opinion not published at this writing.

In the Appendix, Exhibit A, we have set forth relevant excerpts from Chapter 405, Laws Minnesota 1933, including the title and sections numbered 2, 3, 5, 8 and 12.

The taxes claimed due by plaintiff in its causes of action against each of these two defendants include in their measure the sum of $150,044.12 in the case of the Missabe and $214,066.12 in the case of the Iron Range received by them as income from federal securities.

In the Missabe case in its Answer (Substituted) (R. 292) the defendant alleged in Section 8 that there was included in plaintiff's claim" * * * interest received by the taxpayer upon obligations of the United States government in the sum of $150,044.12 which is immune from taxation both under the Constitution of the United States and the Acts of Congress of the United States and under the provisions of the Minnesota State Income Tax Act (Chapter 405, Laws Minnesota 1933)". It was the claim of the state that these federal securities were includable in plaintiff's cause of action and the plaintiff denied the immunity alleged under the Constitution of the United States as well as any immunity under the Minnesota Act.

Similar allegations and claims of immunity were made in the Iron Range case.

The trial court (R. 317) found that the interest above referred to in the Missabe case was included in defendant's income as set forth in plaintiff's amended statement (complaint) and at page (R. 318) in the Conclusions of Law found that defendant was not subject to any payment of any tax on any part of said income. Plaintiff (R. 354) moved the court for the inclusion of said income from federal securities in the sum of $150,044.12. The court (R. 368, f. 1) denied said motion (Assignment No. 25, Transcript page 1609).

Motions for Amended Findings and Conclusions of

Law were also made in the Iron Range case. Motion to Amend Conclusions of Law (R. 1375), Order Denying same (R. 1383), Assignment No. 29 (Tr. page 1628).

The claims of federal constitutional immunity made by defendants were at all times maintained throughout the trial and in the state supreme court and the claims of the state denying such immunity were at all times maintained in the state courts.

It is the contention of the petitioner that the state supreme court expressly and by necessary intendment construed and passed upon petitioner's federal claims with respect to the said federal constitutional immunity of federal securities from the Minnesota tax and that the said federal claims were duly raised and passed upon in said court.

The state supreme court denied plaintiff's claims and decided that defendants were entitled to the federal constitutional immunity with respect to their income from federal securities. The court based its decision upon two grounds, one federal and one non-federal. The court said in the railroad cases, **State v. Duluth, Missabe & Northern Railway Company**, 207 Minn. 618, at page 626, 292 N. W. 401, at page 406:

> "* * * the inclusion of income from tax-exempt securities as a measure of the tax is objectionable when it evidences an attempt to discriminate against income from a particular source."

In support of this basis of its decision, the court cited **Miller v. Milwaukee**, 272 U. S. 713, 47 S. Ct. 280, 71 L. ed. 487; **Schuylkill Trust Co. v. Pennsylvania**, 296 U. S. 113, 56 S. Ct. 31, 80 L. ed. 91. The court said further, same page:

> "The dissent in the latter case said that the discrimination must be either unfriendly in design, or in favor of securities in competition with federal securities included in the tax."

And further, same page:

> "It seems, in the instant case, that to allow taxation of federal government securities under subsection (g) would operate not only as a discrimination, but also as an unfriendly one, to the favor of local securities which are in fact in substantial competition with the federal securities."

The reference to "subsection (g)" has to do with the non-federal ground which we shall now refer to.

The court said, 207 Minnesota at page 626, 292 Northwestern at page 405:

> "Pertinent provisions of c. 405 are subsections (f) and (g) of sec. 12, exemptions from gross income:
>
> "(f) Interest upon obligations of the State of Minnesota, any of its political or governmental subdivisions, any of its municipalities, or any of its governmental agencies or instrumentalities.
>
> "(g) Income received from the United States, its possessions, its agencies, or its instrumentalities, so far as immune from state taxation under federal law."

The court said further, 207 Minnesota at page 626, 292 Northwestern at page 406:

> "Subsection (g) by expressly exempting income from federal securities so far as immune from state taxation under federal law, in effect, provides that such income shall not be included in the measure of the franchise tax. Although a state may constitutionally impose a franchise tax measured by income, including income from tax-exempt securities, Flint v. Stone Tracy Co., 220 U. S. 107, 31 S. Ct. 342, 55 L. ed. 389, Ann. Cas. 1912B, 1312, subsection (g) provides that such income shall not be included as a measure of the tax on the franchise."

Finally at 207 Minnesota 627, 292 Northwestern 406, the court said:

> "We therefore conclude that under any interpretation of subsection (g) income from federal securities should not be included in the measure of the tax on defendants' non-railroad income imposed by c. 405."

Now the remarkable thing about our situation is that subsection (*l*) of Section 12 which was not referred to by the court in its opinion had the effect of entirely removing subsection (g) from the list of exclusions from gross income in the measure of corporate franchise taxation. Subsection (*l*) provided:

> "Subdivisions (c), (d), (i) and (j) shall not apply to corporations, and subdivision (g) shall not apply to corporations taxable under Section 2, except so far as taxable under Section 8.

The corporations here involved are all taxable under Section 2 and are not taxable under Section 8. There is no dispute nor is there any question on that point.

Only corporations taxable under Section 2 pay a franchise tax measured by income. Corporations taxable under Section 3 pay a direct income tax. Section 8 provides for a direct income tax for those corporations whose taxable year expired prior to the effective date of the Minnesota Act, April 21, 1933, but which for subsequent years are required to pay a franchise tax under the provisions of Section 2.

Thus the Minnesota legislature made a careful and deliberate attempt to limit the inapplicability of the exclusion of income from the United States under subsection (g) to those corporations paying a franchise tax rather than a direct income tax.

After the court filed its decision in the railroad cases December 29, 1939, plaintiff called to the court's attention the fact that the court had "*** * * completely overlooked and failed to consider in any way whatsoever subsection (*l*) of section 12 of the Income Tax law. This subsection (*l*) is the one which specifically states that subdivision (g), which refers to the exclusion of income from federal securities in the computation of gross income, shall not apply to corporations.**" (Petition of Ap-

pellant for Rehearing filed January 18, 1940, page 12, Tr. page 1672.)

Plaintiff also at the same time and place called to the court's attention the fact that this point was fully discussed in the state's Supplemental Brief, pages 12-25.

Of course the state supreme court was under no duty to mention or comment upon the governing subsection (*l*). The court had advanced two bases for its decision, one federal, one non-federal. It may have considered its federal ground ample and therefore rested its decision upon that ground.

Following the said Petition of Appellant for Rehearing, the court filed another decision on April 26, 1940, also entitled **State v. Duluth, Missabe and Northern Railway Company,** 207 Minn. 637, 292 N. W. 411 (Tr. 1819 et seq.). In that decision the court made no mention of its omission to comment on subsection (*l*).

We believe that under these circumstances we are entitled to one of two conclusions with respect to the omission of any mention of the governing statutory provision subsection (*l*).

1. The court having advanced two alternative bases for its decision abandoned its non-federal ground when it found that it was entirely mistaken about subsection (g) and that subsection (g) did not exclude defendants' income from federal securities from the tax. This left only one basis, namely, the federal ground.

2. The court ignored subsection (*l*) and continued to base its decision alternatively on the federal and non-federal ground.

Under conclusion No. 1, we are before this court on a federal question because no other question exists.

Under conclusion No. 2, we respectfully submit that we are entitled to have this court examine the Minnesota statute especially section 12 and subsec-

tions (g) and (*l*) to determine whether or not the ignoring of the statutory provisions in such circumstances may not be regarded as essentially arbitrary.

We also submit that in any event such an unusual situation as this constitutes additional support for petitioner's argument that the two grounds advanced by the court are so interwoven that the non-federal ground may not be considered an independent matter.

We believe that the most reasonable explanation that can be furnished for ignoring subsection (*l*) is that the court rested on the federal ground and we are content with that explanation.

If, however, this court finds it necessary to examine further into the alternative bases advanced by the state court, we refer to the cases of **Minnesota v. National Tea Co.**, 60 S. Ct. 678, 309 U. S. 551; **State Tax Commission v. Van Cott**, 59 S. Ct. 605, 306 U. S. 511, 83 L. ed. 950.

We also call to the attention of the court the case of **Enterprise Irrigation District v. Farmers Mutual Canal Company**, 37 S. Ct. 318, 243 U. S. 157, 61 L. ed. 644, in which this court at page 320 of 37 S. Ct. said:

> "But where the non-federal ground is so interwoven with the other as not to be an independent matter or is not of sufficient breadth to sustain the judgment without any decision of the other our jurisdiction is plain."
>
> **"And this is true also where the non-Federal ground is so certainly unfounded that it properly may be regarded as essentially arbitrary,** or a mere device to prevent a review of the decision upon the Federal question." (Emphasis supplied.)

We, therefore, respectfully submit that (even if, under the circumstances, the Minnesota Supreme Court cannot

be said to have abandoned it), the non-federal ground set up in the Minnesota court's decision is so arbitrary and unfounded that it should not be considered as an adequate independent non-federal ground.

THE QUESTIONS PRESENTED.

QUESTION I.

The Minnesota Corporate Franchise Tax Act, Chapter 405, Laws 1933, is measured by net income and determined by gross income. Railroad and other gross income is differentiated, the distinction between them being "income derived from the exercise of the corporate franchise within the scope of railroad ownership or operation and that from its exercise without such scope." In 1933, pursuant to the Act of Congress of June 16, 1933, "Emergency Railroad Transportation Act 1933", 48 Stat. 220, defendant received from the United States $7,774,804.19 belonging to the United States, to which defendant, prior to said Act of Congress, had no title or interest legal or equitable.

Of this amount of $7,774,804.19, the sum of $5,808,256.61 consisted of trust funds belonging to the United States, held by defendant as trustee for the United States, transferred to the United States at various times during the years 1924 to 1930, pursuant to the Act of Congress of February 28, 1920, "Transportation Act 1920", 40 Stat. 488.

The question is whether or not the receipt of said sum of $5,808,256.61 by defendant under the provisions of said Act of Congress of June 16, 1933 constitutes gross income derived from the exercise of defendant's corporate franchise without the scope of railroad ownership or operation.

QUESTION II.

(The first paragraph of Question II is the same as the first paragraph of Question I and is here omitted for sake of brevity.)

Of this amount of $7,774,804.19, the sum of $1,966,547.58 consisted of accretions or earnings on moneys belonging to the United States, and which had never at any time been in the hands of the defendant.

The question is whether or not the receipt of said sums of $1,966,547.58 by defendant under the provisions of said Act of Congress of June 16, 1933, constitutes gross income derived from the exercise of defendant's corporate franchise without the scope of railroad ownership or operation.

QUESTION III.

All of the voting stock of defendants is owned by and under the legally enforceable control of the same interests. Section 32 (c) of Chapter 405, Laws Minnesota 1933, provides that:

> "* * *. If 90 per cent of all the voting stock of two or more corporations is owned by or under the legally enforceable control of the same interests the Commission may impose the tax as though the combined entire taxable net income was that of one corporation except that the credit provided by Section 27 (e) shall be allowed for each corporation; but inter-company dividends shall in that event be excluded in computing taxable net income." (Emphasis supplied.)

The Tax Commission assessed the tax separately on each corporation. It did not assess on a combined basis.

The question is whether or not the word "may" in said provision, when given its natural permissive meaning, renders said provision repugnant to the equal protection clause of Section 1 of the Fourteenth Amendment, Constitution of the United States.

QUESTION IV.

The question is whether or not Section 12, Chapter 405, Laws of Minnesota 1933, which provides for the inclusion of income from federal securities together with income from all other securities, with the sole exception of income from Minnesota state and local securities, in the measure of the Minnesota Corporate Franchise Tax, is repugnant to the immunity of federal securities from state taxation under the Constitution of the United States.

ASSIGNMENTS OF ERROR.

For the sake of brevity, we here refer to the Assignments of Error set forth in our Brief infra following the said Questions and the Points thereunder.

THE REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT.

There are special and important reasons why a review on Writs of Certiorari in these cases should be granted in the sound discretion of the court. In addition to the facts and argument submitted in our Petition and Brief, we urge further:

that the five actions before the court involved more than $400,000 of taxes for the year 1933;

that other substantial amounts for subsequent years are indirectly involved in connection with the questions relating to consolidated return;

that other substantial amounts of taxes of other large corporations are also indirectly involved in connection with the questions relating to consolidated return;

that other substantial amounts of taxes of other large corporations are also indirectly involved in connection with the question relating to the inclusion of income from federal securities in the measure of the Minnesota Corporate Franchise Tax;

that the state supreme court has decided federal questions of substance not heretofore determined by this court;

that the state supreme court has decided federal questions of substance in a way not in accord with applicable decisions of this court;

that the questions here presented are questions of substance.

WHEREFORE, your petitioner prays that Writs of Certiorari be issued out of and under the seal of this Honorable Court directed to the Supreme Court of the State of Minnesota commanding that court to certify and send to this court for its review and determination a full and complete transcript of the record and all proceedings in the said Supreme Court had in the cases numbered and entitled on its docket, respectively, No. 32125, State of Minnesota vs. Duluth, Missabe and Northern Railway Company, and Duluth, Missabe and Iron Range Railway Company; No. 32124, State of Minnesota vs. The Duluth and Iron Range Rail Road Company and Duluth, Missabe and Iron Range Railway Company; No. 32126, State of Minnesota vs. Spirit Lake Transfer Railway Company and Duluth, Missabe and Iron Range Railway Company; No. 32312, State of Minnesota vs. Oliver Iron Mining Company; and No. 32313, State of Minnesota vs. Proctor Water & Light Company; to the end that the decisions and judgments of said Supreme Court of the State of Minnesota and each of them may be reviewed and reversed by this Honorable

Court and that judgments may be entered for the State of Minnesota in each of said actions.

STATE OF MINNESOTA,
By J. A. A. BURNQUIST,
Attorney General of the State of Minnesota,
Counsel for Petitioner,
102 State Capitol, St. Paul, Minnesota.

JOHN A. PEARSON,
Special Attorney for
the State of Minnesota,
E-901 First Natl. Bk. Bldg.,
St. Paul, Minnesota.

IRVING M. FRISCH,
Special Attorney for
the State of Minnesota,
416 Hodgson Bldg.,
Minneapolis, Minnesota.
Of Counsel for Petitioner.